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IN THE

Supreme Court of the United States

October Term, 1964

No. 893

ARTHUR HOFFMAN,

Petitioner,

against

CHRYSLER CORPORATION, ET AL., and PAUL C. ACKERMAN, ET AL.,

Respondents, Defendants below,

and

SOL A. DANN, ET AL., and MARY L. GALLO, ET AL.,

Respondents, Plaintiffs below,

and

ERWIN H. EZZES, HERMAN KOENIGSBERG and VIRGINIA S. JUDSON, ET AL.,

Respondents, Objectors below.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF DELAWARE

BRIEF OF RESPONDENTS, MARY L. GALLO AND A. JAMES GALLO, IN OPPOSITION

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Opinions Below

The opinions of the Court of Chancery of the State of Delaware are reported as *Dann* v. *Chrysler Corporation*

in 198 A. 2d 185 (1963) [Gallo A1-41]*. The opinion of the Supreme Court of the State of Delaware, affirming the judgment of the Court of Chancery, is reported as *Hoffman* v. *Dann* in 205 A. 2d 343 (1964) [Pet. A9-30].

Jurisdiction

The petitioner claims that the jurisdiction of this Court is founded on 28 U. S. C. § 1257(3). He contends that federal questions are raised involving abridgement by the Supreme Court of Delaware of the "privileges and immunities" and "due process of law" clauses of the Fourteenth Amendment to the Constitution of the United States.

The Gallo respondents submit that there is an absence of jurisdiction for this Court to entertain the instant petition since petitioner did not assert any alleged abridgement of his constitutional rights either before the Supreme Court of Delaware or before the Chancery Court of Delaware; and further, because he raises no federal question in his present petition.

Questions Presented

The proceedings before the Delaware courts involved a determination of the fairness and propriety of a proposed settlement of two stockholders' derivative actions

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* References will be made to the Appendices to this brief (Gallo A), to petitioner's brief (Pet. A), and to the printed appendix of the defendants-appellees in the court below (A). References to portions of the Transcript of the settlement hearing not printed in the appendix of the defendants-appellees in the court below will be T references. Docket entry references will be denominated S. Ct. Dkt. # , for those of the Supreme Court of Delaware; Gallo Dkt. # , for those of the Gallo action in the Court of Chancery; and Dann Dkt. # , for those of the Dann action in the Court of Chancery. Gallo exhibits will be referred to as GX and defendant exhibits as DX.

which had been instituted in the Court of Chancery of Delaware in behalf of Chrysler Corporation (hereinafter "Chrysler") for alleged waste and mismanagement. No federal statute is involved on the instant petition. Chrysler is a Delaware corporation. Both the adjectival and substantive laws of Delaware are applicable.

The petitioner predicates his application for certiorari on the grounds that the Delaware courts did not permit the objecting stockholders to try the issues of the case on the merits and that the Delaware courts failed to follow decisions of this Court relating to claims of fraud and the judicial inquiry thereon.

The Gallo respondents will presently demonstrate:

1. That petitioner did not cite as error to the Delaware courts any violation of the Constitution of the United States. Petitioner now for the first time anywhere contends in his present petition that there has been an abridgement of rights under the Fourteenth Amendment.

2. That there is no federal question involved:

(a) The Delaware courts afforded all parties and stockholders of Chrysler, including petitioner and the other objecting stockholders, full opportunity to be heard, upon due notice, as to the fairness and propriety of the proposed settlement, in accordance with established judicial procedures.

(b) The petitioner and his attorneys neglected to avail themselves of their right to be heard by failing to attend any of the settlement hearings before the Chancellor except for one pre-testimony session, or to submit any substantive post-hearing brief. They further failed to attend the hearing on oral argument of the several appeals to the Supreme Court of Delaware, including petitioners's own appeal to that court.

(c) The Court of Chancery made a thorough inquiry into the fairness and propriety of the proposed settlement.

(d) The petitioner is seeking to have this Court review the determinations of the Delaware courts with respect to Delaware law.

(e) There is ample support in the record for the approval of the proposed settlement by the Delaware courts.

Counter-Statement of the Facts

The petitioner's statement of the facts contains many errors. A counter-statement is necessary.

A. History of the Litigation.

The Delaware litigation involved two stockholders' derivative actions. The first was instituted by respondent Dann and certain other plaintiff stockholders on August 12, 1960 (Dann Dkt # 1). Until December 7, 1961, there were various determinations of motions relating to pleadings and discovery, including the decisions of the Chancellor in *Dann* v. *Chrysler Corporation* reported in 166 A. 2d 431 and 174 A. 2d 696. The defendants sought discovery of relevant documents in Dann's files which Dann had stated on various occasions contained information relating to misconduct of defendants (A287-335). Under direction of the Chancellor, subject to safeguards for privileged documents and the names of alleged informants, Dann produced, as he averred, "all material relevant to the issues involved in the complaint, as amended, in this suit, received by him prior to January 1, 1961" (A330). His own attorney had inspected the documents in Dann's files for three days and "separated out what I considered pertinent to the complaint as then amended" (A329, 309-310). Those documents were thereafter filed with the Court of Chancery and formed part of the record on the settlement (A388).

On February 23, 1962, the Gallo plaintiffs instituted their derivative action (Gallo Dkt. # 1). Procedural activities affecting both actions then followed. Finally, by order dated June 14, 1962, the Chancellor consolidated the two actions solely for the purposes of discussing possible settlement (Gallo A2). Subsequently, the time originally fixed for such discussions was extended at the request of the parties (Gallo A2).

The proposed settlement was the end product of arm's length bargaining between the plaintiffs and the defendants in the context of the claims asserted, the defenses interposed and the final disposition of the total litigation. The intense negotiations covered more than one year and until the very end there was no certainty that the final result of settlement would be accomplished (A122-132).

Throughout the course of the litigation from the time that it was instituted, the Gallo action was separate and independent from the Dann action (A455). Counsel for the Gallo plaintiffs, with the assistance of an accounting expert and adviser, actively and independently participated in the negotiations for settlement (A455-456, 169). The Gallo plaintiffs and their counsel reached an independent judgment that the ultimate settlement was fair and reasonable (A455-456). Their judgment, as well as that of counsel for the plaintiffs in the Dann action, was based upon elaborate discovery (Pet. A9; Gallo X600).

Petitioner, in his statement of the facts, completely overlooks the participation by the Gallo plaintiffs in the settlement negotiations. He would have this Court believe that Dann alone negotiated the settlement with the defendants. This is plain error. In fact, counsel in the Dann action were not negotiating solely for Dann but also for his co-plaintiffs in the Dann action. Dann did participate in the settlement negotiations and his law partner was one of the signatories to the settlement agreement (A40).

The proposed settlement is contained in the Stipulation of Settlement dated March 5, 1963 (A31-42). The heart of the settlement is the modification of the Chrysler Incentive Compensation Plan (Gallo A4). Charges of unfairness in the application of the old formula under that Plan are alleged in paragraph 107 of the Gallo complaint (A69) and paragraphs 202 and 204 of the Dann complaint (A52-53). The differences between the old and new formulae are analyzed in the decisions of the Delaware courts (Gallo A25-29; Pet. A23-24).

It was the considered opinion of plaintiffs' attorneys in their evaluation, after discovery proceedings, of the causes of action pleaded in the Dann and Gallo complaints that (1) charges of personal interest and personal profit on the part of the individual defendants (except Newberg) were not sustained by the evidence and this would not permit a successful prosecution of them; (2) charges of mismanagement lay primarily within the area of business judgment, and although criticisms might be levelled at some of the transactions questioned, the burden of proving culpability on the part of the defendants was too great to promise success in the prosecution of those charges; and also brought into the balance were the management changes and the then recent management accomplishments. As to charges of unfairness of the Incentive Compensation Plan, plaintiffs' attorneys believed they were well grounded and a revision of the Plan was necessary to prevent awards unless the officers and employees should produce results of a magnitude which would merit their participation with stockholders in earnings, and the rewards should then be scaled to the measure of accomplishment (A8-9).

B. Proceedings in the Court of Chancery of Delaware on the Proposed Settlement.

After the Stipulation of Settlement was filed, pursuant to the Chancellor's order, a court-approved Notice of Settlement was mailed to each stockholder of Chrysler (A7-30).

The elaborately detailed Notice was enclosed with the Proxy Statement (DX300) for the Annual and Special Meetings of Chrysler stockholders held on April 16, 1963, at which, *inter alia*, the Chrysler stockholders were to vote on the proposed modification of the Incentive Compensation Plan (DX 300, Exh. "C"), subject to Court approval of the proposed Settlement (Gallo A4-5). The stockholders were advised in the Proxy Statement that a vote in favor of the Plan modification "will, in effect, be a vote in favor of the settlement" (Gallo A3; DX300, p. 20). The stockholders overwhelmingly favored the settlement and the proposed Plan modification by the vote of 6,699,016 (or 97.89% of those voting) to 144,244 (A79).

At the time, petitioner Hoffman held 10 shares of Chrysler stock (Dann Dkt. #180). He would at the present time have been the holder of 40 shares of the stock because of the effect of two 2 for 1 stock splits that occurred in the interim. However, after the settlement hearings, he disposed of part of his holdings, so that he presently owns only 20 shares of Chrysler stock (Gallo A44).

Prior to the opening of the settlement hearings on May 13, 1963, various objectors, including petitioner Hoffman (Dann Dkt. #180), filed notices of intention to object.

Dann, however, again raised the matter of the documents in his files which he contended contained information as to misconduct by defendants.

A pre-trial hearing was held before the Chancellor on April 11, 1963, at which the matter of the Dann documents was further considered (A356-374). The court concluded that the hearing on the settlement should proceed as scheduled.

The Gallo plaintiffs took immediate steps to determine whether Dann in fact had any evidence in his files. They had believed that the heart of Dann's documents had been theretofore produced by him on the defendants' discovery

of his papers. Such documents had been considered in connection with the settlement negotiations. Accordingly, the Gallo plaintiffs moved for the production of all of the documents in Dann's files to which he adverted and they also noticed the deposition of Dann (A377-379). Dann objected to any further production and to the taking of his deposition (A381-383). The Chancellor ultimately directed that Dann produce the documents for inspection and that he appear to testify at the settlement hearing on May 13, 1963 (A393-396).

All of the Dann documents were produced at the settlement hearing for inspection. Full right and opportunity were afforded to all parties and all objectors or their attorneys to inspect those documents (A396, 397-401, 402-408, 421). They were inspected by attorneys for the Gallo plaintiffs through two full days and two night sessions, and on a third day through the late afternoon (A408). In addition, attorneys for objector Ezzes, for Chrysler and for certain of the other defendants also inspected the Dann documents during that period (A453-457).

While petitioner Hoffman and his attorneys had the same right and opportunity of inspection, they did not see fit to exercise that right (A454-455).

The attorneys for the Gallo plaintiffs presented an oral report to the Chancellor during the settlement hearing with respect to their inspection of the Dann documents, concluding that:

> "In essence, the material is of the same kind and nature as the material heretofore filed by him (Dann) with this Court, which contained the heart of his documents at the time. We are of the opinion, as the result of our inspection, and we so represent to this Court, that the Dann documents do not comprise evidence. Accordingly, the Gallo plaintiffs adhere to their position, proposing the Court approval of the settlement of this litigation as submitted." (A408-409)

Dann also testified at the settlement hearing and was cross-examined by the attorney for objector Koenigsberg (A410-421). Here again, petitioner Hoffman and his attorneys had full opportunity to cross-examine Dann but did not see fit to do so. Dann testified in support of the proposed settlement and conceded that his documents did not contain admissible evidence (A410-421).

The Chancellor granted the objectors the widest latitude of discovery and call of witnesses at the settlement hearing (A458). The court delved deeply into each cause of action which any of the objectors considered might have merit (A459). The objector Ezzes contended that a large number of the causes of action had substantial merit. As the decisions of the Chancellor and the Supreme Court of Delaware attest, objector Ezzes' presentations of evidence and argument were carefully considered in every respect and were found to be without substance (Gallo A10-24; Pet. A11-21). The other objectors concurred with the plaintiff's attorneys in most regards in their evaluation of the causes of action apart from the Incentive Compensation Plan cause (Gallo A7).

As to the proposed modification of the Incentive Compensation Plan itself, the record is replete with exhibits and testimony offered at the settlement hearing attesting to the improvement of the new formula over the old (A94-106; 248-265; DX308-311). The highest echelon of Chrysler executives was closely examined and at length with regard to the modification and the settlement negotiations that led to it (A94-106, 132-133; 143, 156, 248-265).

In addition, prior to the hearing the Chancellor appointed an *Amicus Curiae* to inquire into and report on what appeared to be the issues relevant to the proper consideration of the proposed settlement and the proofs which would be of assistance to the court. A lengthy and detailed report was submitted (Gallo A3; Pet. A10).

The following witnesses gave testimony at the hearing:

Walter J. Simons	Treasurer of Chrysler	T. 29-243
George H. Love	Chairman of the Board of Chrysler	T. 248-358
Lynn A. Townsend	President of Chrysler	T. 373-565
Gwain H. Gillespie	Partner of Touche, Ross, Bailey & Smart, Certified Public Accountants, in charge of Chrysler audit	T. 582-629 T. 708-714
Emlyn Lloyd	Director of Supplier Relations, Purchasing Department of Chrysler	T. 630-671
Robert G. Page	Director of Chrysler and Chairman, Incentive Compensation Committee	T. 673-707
Lester L. Colbert	Former President and Chairman of the Board of Chrysler	T. 715-827
Kaufman T. Keller	Former President and Chairman of the Board of Chrysler	T. 829-838
Keith A. Jenkins	Attorney on legal staff of Chrysler	T. 842-866
Sol A. Dann	A plaintiff in the Dann action	T. 891-915
William H. Ryan	Certified Public Accountant, for Objector Koenigsberg	T. 917-950
Francis S. Bensel	Partner of Kelley Drye Newhall Maginnes & Warren	T. 951-964

In addition to the comprehensive testimony, including cross-examination, of the foregoing witnesses, and the voluminous exhibits introduced at the hearing, the record also contains the depositions taken by the plaintiffs in the discovery proceedings prior to final settlement (Gallo X600). Ten witnesses were then examined—George T. Higgins, Secretary of Chrysler; Louis B. Warren, director of Chrysler and partner of Kelley Drye Newhall Maginnes & Warren; Francis W. Misch, director and Vice President—Finance of Chrysler; Emlyn Lloyd; Lester L. Colbert; Paul C. Ackerman, director and Vice President—Engineering; Richard D. Morrison, Purchasing Agent—Materials and Supplies of Chrysler; Rinehart S. Bright, director and Vice President—Operations Staff; Kaufman T. Keller; and Robert P. Laughna, former executive of Chrysler.

Petitioner Hoffman and his attorney failed to attend any of the settlement hearing trial sessions, although he had filed objections and appeared as an objector. His attorney attended only one pre-trial session on May 1, 1963 (Dann Dkt. #213). The pre-trial sessions were held on April 11, 1963 (A356), April 18, 1963 (A384), May 1, 1963 (Dann Dkt. #213), and May 6 and 7, 1963 (A396; Dann Dkt. #231). The settlement hearing trial sessions were held on May 13, 14, 15, 16, 17 and 20, 1963 (T. Vols. I-III; Dann Dkt. #233-235).

After the close of the settlement hearing, extensive briefs were filed by the proponents and the objectors (Gallo A4), except petitioner Hoffman. His brief consisted of only two pages without any substantive presentation (Gallo A42).

On December 31, 1963, the Chancellor filed his decision approving the settlement subject to a limited condition, which was complied with by the defendant directors involved (Gallo A1-38).

Applications were made by objectors Ezzes, Koenigsberg and Sandler for reargument, which were denied by the

Chancellor in his supplemental opinion of February 7, 1964 (Gallo A38-41).

After testifying at the settlement hearing Dann asked to be "excused permanently" and for leave to take back to Detroit the documents which he had produced. The request was granted by the court (A421). Nevertheless, after the Chancellor's decision, Dann once again appeared before the court on an application by him, *inter alia*, to reopen the settlement. The application was heard by the Chancellor on February 7, 1964 (A431-448). The core of his contentions at that late juncture was basically a reiteration of his previous positions with respect to the documents which he had produced at the settlement hearing (A431-440). In effect, Dann was seeking reexploration of matters that had been theretofore thoroughly explored by the Chancellor at the settlement hearing and at the pre-trial hearings (A444). Dann, significantly, did not repudiate his testimony at the settlement hearing (A438). The court reaffirmed its determination that the settlement was arrived at in good faith and denied Dann's application (A446-447).

Thereafter, by motion filed on February 24, 1964 (Dann Dkt. #282; Gallo Dkt. 98), at the tail end of these exhaustive proceedings, petitioner Hoffman appeared. He had not seen fit to participate actively as an objector or even to be represented independently at the sessions, of the settlement hearing. Nevertheless, he now sought a variety of reliefs. He sought intervention, the right of discovery including depositions by his attorneys of Dann and all of the defendants named in both actions (some 100 individuals and corporations) and the production of all books, records and documents relevant to the issues in the case, and a stay of the settlement (Gallo A43). He requested ninety days for the discovery. Hoffman was afforded a hearing on this matter before the Chancellor on February

24, 1964 (A449-461). In his motion papers, Hoffman made the following averment (Gallo A44):

> "I must confess to the Court that my specific knowledge of the charges involved has been derived from a reading of the Dann and Gallo complaints and from the proceedings in connection with the proposed settlement. I have no personal knowledge of the matters involved nor have I taken any depositions in connection therewith."

Hoffman predicated his motion entirely on Dann's previous application to reopen the settlement (A449-450). After hearing, the court reaffirmed its determination that the settlement was fair and entered into in good faith, and denied Hoffman's motion except that he was granted leave to intervene as a party plaintiff for the sole purpose of objecting to the fairness and adequacy of the settlement (A460). Final decree and judgment approving the settlement was filed on March 9, (Gallo Dkt. #105; Dann Dkt. #301).

C. Appellate Proceedings in the Supreme Court of Delaware.

The objectors, including Hoffman, appealed to the Supreme Court of Delaware. Dann did not appeal. Briefs were submitted by all interested parties. The petitioner's statement in his brief to this Court that he argued "the Constitutional questions involved" before the Supreme Court of Delaware is clearly not so. In neither his ten-page principal brief (S. Ct. Dkt. #4) nor in his seven-page reply brief (S. Ct. Dkt. #17) did Hoffman raise any constitutional question or in fact even mention the Constitution.

Only two questions were raised by Hoffman in his brief to the Supreme Court of Delaware. The first related to the type of intervention granted to him by the Court of Chancery. The second related to his contention that the record appeared to him to be insufficient to permit a proper determination as to the fairness and adequacy of the settle-

ment and sought remand for further consideration at hearings (Hoffman Brief, p. 2). On September 21, 1964, the Supreme Court heard oral argument on the appeals. Neither Hoffman nor his attorneys appeared. Attorneys for all other parties were present and argued orally before the court. In a comprehensive decision, the Supreme Court of Delaware unanimously affirmed the judgment of the Chancellor approving the settlement (Pet. A. 9-30). Petitions for reargument were thereafter denied (Pet. A. 31-32). Hoffman did not petition for reargument.

ARGUMENT

I

No constitutional question was set up or claimed by petitioner in the Delaware courts.

The jurisdiction of this Court to review the final judgment of the Supreme Court of Delaware in the first instance depends upon whether the petitioner "specially set up or claimed" any constitutional question and brought such claim and the grounds therefor to the attention of the Delaware courts with fair precision. *New York ex rel. Bryant v. Zimmerman*, 278 U. S. 63, 67 (1928).

In *Oxley Stave Co.* v. *Butler County*, 166 U. S. 648, 655 (1897), this Court referred to the requirements of particularity in this respect, stating:

> "* * * the jurisdiction of this court to re-examine the final judgment of a state court cannot arise from mere inference, but only from averments so distinct and positive as to place it beyond question that the party bringing a case here from such court intended to assert a Federal right."

In none of the papers filed by petitioner Hoffman in either the Court of Chancery or the Supreme Court of Dela-

ware, nor in his oral presentation to the Chancellor on his motion heard on February 24, 1964, did he even refer to the Constitution of the United States, or to the Fourteenth Amendment, or to any specific clause of the Fourteenth Amendment, or to any violation thereof by the Delaware courts. Petitioner Hoffman did not in the slightest apprise the Delaware courts that he was raising a federal question or that he was claiming any abridgment of rights under the Constitution of the United States. Therefore, the prerequisite to jurisdiction of this Court is lacking, and no jurisdiction attaches. *Herndon* v. *Georgia,* 295 U. S. 441, 442-3 (1935); *Harding* v. *Illinois,* 196 U. S. 78, 88 (1904); *Capital City Dairy Co.* v. *Ohio,* 183 U. S. 238, 248 (1902); *Oxley Stave Co.* v. *Butler County, supra; Bowe* v. *Scott,* 233 U. S. 658, 664-5 (1914).

Petitioner states in his petition to this Court, at page 4, that the Supreme Court of Delaware in its decision completely ignored the Constitutional questions raised by him. The plain fact is that he raised none for the Supreme Court of Delaware to determine. *Mutual Life Ins. Co.* v. *McGrew,* 188 U. S. 291, 309 (1903). Furthermore, petitioner did not apply to the Supreme Court of Delaware for reargument.

II

No federal question is raised by the petition herein.

It is submitted that both from jurisdictional and substantive aspects, no federal question is raised by the petition.

A. The Delaware Courts Followed Well-Established Judicial Procedures in the Cases at Bar in Full Compliance With the Requirements of Due Process of Law.

Under the first "question presented", petitioner asserts that failure to try the issues on the merits violated the due process of law clause of the Fourteenth Amendment.

This is patently unsound and is not the law of the land. On the contrary, the law favors the settlement of disputed claims. *Keller* v. *Wilson & Co.*, 194 Atl. 45, 47 (Del. Ch., 1937); *Winkelman* v. *General Motors Corp.*, 48 F. Supp. 490, 495 (S. D. N. Y., 1945). "The very purpose of a compromise is to avoid the determination of sharply contested and dubious issues." *In re Prudence Co.*, 98 F. 2d 559, 560 (2nd Cir., 1938), cert. den. *sub nom. Stein* v. *McGrath*, 306 U. S. 636 (1939).

Rule 23(c) of the Federal Rules of Civil Procedure contemplates settlement of stockholders' derivative suits. Rule 23(c) provides for the judicial procedure to be followed on such settlements. The Court of Chancery of Delaware adopted the Federal Rules, and Rule 23(c) of the Rules of the Court of Chancery is substantially the same as Rule 23(c) of the Federal Rules (Vol. 13, Del. Code Ann., Court Rules). The Supreme Court of Delaware expressly stated that the Court of Chancery approved the settlement under Rule 23(c) (Pet. A. 26).

In the cases at bar, the Chancellor fully complied with Rule 23(c) and with all aspects of due process. A detailed Notice of Settlement, approved in form by the court, was mailed to all stockholders of Chrysler advising them of the proposed settlement and of their rights to object thereto, to undertake broad discovery, and to inspect all of the records on file (including exhibits and depositions), and to be heard at the settlement hearing at the specified date, time and place. As set forth in the Counter-Statement of Facts herein, the Chancellor afforded objectors the widest scope of discovery and call of witnesses at the hearings. The petitioner Hoffman had due notice and full opportunity to be heard. There was complete adherence by the Court of Chancery to the requirements of due process of law. *Pennoyer* v. *Neff*, 95 U. S. 714, 733 (1877); *Anderson National Bank* v. *Luckett*, 321 U. S. 233, 246 (1943).

Petitioner cites *Chambers* v. *Baltimore & Ohio R.R. Company,* 207 U. S. 142 (1907) for the proposition that where a party is not given the right to litigate a claim on the merits in state courts, the privileges and immunities clause of the Fourteenth Amendment is abridged. The *Chambers* case does not hold any such proposition. In fact, this Court in *Chambers* upheld the Ohio courts in denying access to a citizen of any State (including Ohio) to its courts under a "wrongful death" statute, where the decedent was not a citizen of Ohio and the wrongful act causing death occurred in another State. The "equal treatment" clause of Article IV, section 2, paragraph 1, of the Constitution of the United States was involved in that case, not the Fourteenth Amendment.

Petitioner also cites *Prudential Insurance Company* v. *Cheek,* 259 U. S. 530 (1922), for a rule that where state courts deny a party the right to assert a claim or defense, such conduct constitutes deprivation of property without due process of law. No such rule is propounded in that case. This Court in *Prudential* upheld the constitutionality of a "Service Letter Act" as not being repugnant to the "due process of law" and "equal protection of the laws" clauses of the Fourteenth Amendment.

On the other hand, in *Perrine* v. *Pennroad Corporation,* 47 A. 2d 479, 486, 489 (Del. S. Ct., 1946), the Supreme Court of Delaware was explicit in its holding that in proceedings for the settlement of a stockholder's derivative suit, the Court of Chancery was not required to try the case on the merits, and that there was no violation of the Fourteenth Amendment by the lower court's refusal to admit all of the evidence offered by the objectors concerning the merits of the case.

B. The Petitioner, Having Been Afforded a Full Opportunity to be Heard at the Settlement Hearing and Neglecting to Avail Himself Thereof, May Not Claim That He Was Deprived of Any Constitutional Right by an Adverse Determination.

At the hearing on the petitioner's post-decision motion before the Chancellor, the following statements to the court by counsel are significant:

> "Mr. Corroon: * * * Now with respect to Mr. Bader's application, your Honor will recall that Mr. Bader attended one day of a hearing before your Honor and thereafter never saw fit to set foot in this court until today. He had the opportunity to participate in the rather lengthy hearings that were held last May. He did not see fit to do so. The matters that Mr. Dann refers to, many, many of them are matters that were covered by the allegations of the complaint, and Mr. Bader was able, if he had so wished, to cross-examine the witnesses that we put on the stand last May. He was so little interested in the matter that he never showed up. * * * " (A451-452)
>
> * * *
>
> "Mr. Bader: May it please your Honor, I would just like to say one thing in respect to what Mr. Corron said about my appearances at the various hearings. Of course, Mr. Corroon is absolutely correct in what he stated. * * * " (A457)

Under the broad discovery granted by the Chancellor to objectors, the petitioner had the right to examine fully into the fairness and propriety of the settlement, to interrogate witnesses both before and during the settlement hearing, and to inspect all of the Dann documents. Other objectors availed themselves of these rights. Nothing of any substance was raised after decision that had not been in issue before the Chancellor prior to the decision (A452-459).

Our jurisprudence does not permit a party to frustrate the forward progress of judicial process by sleeping on his rights and after determination to awaken and seek to undo all that has transpired. Neglecting to avail himself of his rights, the petitioner may not now claim that he was deprived of any constitutional right. *Southern Ry. Co.* v. *Durham*, 266 U. S. 178 (1924); *Hallberg* v. *Goldblatt Bros.*, 363 Ill. 25, 1 N. E. 2d 220 (1935); *Narragansett Amusement Co.* v. *Riverside Park Amusement Co.*, 260 Mass. 265, 157 N. E. 532, 535 (1927). The due process of law clause does not guarantee more than one hearing before judgment at which to be heard and present evidence. Petitioner had that hearing and opportunity before the Chancellor. *Southern Ry. Co.* v. *Durham, supra; Brein* v. *Conn. Eclectic Examining Board*, 103 Conn. 65 130 Atl. 289, 295 (1925), error dismissed for want of jurisdiction, *sub nom. Brein* v. *State Dept. of Health*, 273 U. S. 640 (1926); *Black* v. *York*, 300 Ky. 166, 189 S. W. 2d 599, 600 (1945).

C. The Court of Chancery Made a Thorough Inquiry Into the Fairness and Propriety of the Proposed Settlement Under Applicable Delaware Law; and There is Ample Support in the Record for the Approval Thereof by the Delaware Courts.

The statements in the petition that the Delaware courts did not consider the good faith aspect of the settlement is not true. As set forth in the Counter-Statement of Facts in this brief, the Chancellor's approach to the procedures to be followed in the settlement hearing was designed to make certain that the settlement was arrived at in good faith. The Chancellor had occasion on petitioner's post-decision motion to make this point clear:

> "All I can say is that feeling as I do, a great responsibility to see that the settlement is only approved if it is fair and in good faith, I have found nothing in the matters presented to me which would justify further hearings or modification of this settlement." (A458-9)

Moreover, the petitioner totally ignores the fact that the Gallo plaintiffs and their counsel were an independent force in the settlement negotiations, entirely separate and apart from the Dann plaintiffs and their counsel (A454-7). The record contains no charge of any nature from any source, including Dann himself, that the Gallo plaintiffs and their counsel did not negotiate in good faith or that their conclusion as to the fairness of the settlement was not an independent exercise of their own judgment (A455-7). This was also recognized by the Chancellor in his decision approving the settlement (Gallo A37).

The petitioner cites, at page 7 of his petition, three decisions of this Court, namely, *American United Mutual Life Insurance Co.* v. *City of Avon Park,* 311 U. S. 138 (1940); *Twin-Lick Oil Co.* v. *Marbury,* 91 U. S. 587 (1875); and *Strong* v. *Repide,* 213 U. S. 419 (1909), for what he asserts are holdings by this Court that failure of a court to investigate any possibility of fraud in connection with the settlement of stockholders' derivative actions constitutes a violation of Constitutional provisions. That is plainly a misstatement of the holdings in those cases. The Constitution of the United States is not even referred to in any of those decisions. None of the three cases involved a stockholders' derivative action.

American United involved the applicability of provisions of Chapter IX of the Bankruptcy Act to a plan of composition. *Twin-Lick* involved an appeal to this Court from the Supreme Court of the District of Columbia on general substantive law only. This Court affirmed a decree in favor of the defendant, upon a holding that there had been no breach of fiduciary duty or concealment in the sale of property. *Strong* similarly involved substantive law only on an appeal to this Court from the Supreme Court of the Philippine Islands. In applying Philippine law, this Court concluded that the sale of stock there involved in private litigation was fraudulent.

Petitioner asserts, at page 7 of his petition, that the cases of *Feldman* v. *Pennroad Corp.*, 155 F. 2d 773 (3rd Cir., 1946); *Perrine* v. *Pennroad Corp., supra,* 47 A. 2d 479 (Del. S. Ct., 1946); *Braun* v. *Fleming-Hall Tobacco Co.*, 92 A. 2d 302 (S. Ct., Del., 1952); and *Karasik* v. *Pacific Eastern Corp.*, 180 Atl. 601 (Del. Ch., 1935), follow the same rule which he ascribed to the three cases of this Court discussed above. Actually, these four latter cases, so far as pertinent, set forth the law of Delaware in its application to the settlement of stockholders' derivative suits. That law in part provides that the Delaware courts will set aside a proposed settlement if negotiated in bad faith. No constitutional question was involved in any of the four cases in that respect.

Significantly, however, the federal court in *Feldman* dismissed a complaint in which a stockholder sought to enjoin Pennroad from consummating the proposed settlement of a stockholders' derivative suit and to appoint a receiver to prosecute all claims in its behalf. The settlement of that suit had been approved by the Court of Chancery and the approval affirmed by the Supreme Court of Delaware in *Perrine* v. *Pennroad, supra.* The particular stockholder had appeared as an objector in the settlement hearing before the Court of Chancery. The federal court held in *Feldman* that the plaintiff was estopped from further disputing the settlement.

In *Braun*, the conduct of the objector is analogous to that of the petitioner in the case at bar. Braun had been afforded the opportunity at the settlement hearing to examine principal witnesses, to take depositions of any witness and to take any other steps toward controverting the proposed settlement. He did not avail himself of the opportunity. Braun urged what would have been tantamount to a trial of the action. In rejecting Braun's position, the Supreme Court of Delaware pertinently stated:

> "One of the considerations which anciently caused the law to favor objects designed to put an end to

> litigation was the saving of time, expense, and inconvenience incident to trial. * * * Since Braun's counsel did nothing to take advantage of that opportunity, it would have been an unwarranted imposition upon all of the parties if the Chancellor had acceded to the demand that he require what would be tantamount to the very trial which this settlement was designed to avoid" (92 A. 2d, pp. 309-10).

Finally, petitioner cites the dissenting opinion in *Masterson* v. *Pergament*, 203 F. 2d 315 (6th Cir., 1953). However, aside from the irrelevancy here of that opinion, the majority of the court there affirmed approval of the settlement; and this Court denied certiorari, 346 U. S. 832 (1953).

It is apparent that petitioner is actually seeking to have this Court review the application of Delaware law by the Delaware courts. This Court in numerous decisions has held that it will not review State law absent a federal question, even if the state courts have erred in the application of their own law, which surely is not the case in the matter at bar. *Enterprise Irrigation District* v. *Farmers Mutual Canal Company*, 243 U. S. 157 (1917); *Arrowsmith* v. *Harmoning*, 118 U. S. 194 (1886); *Iowa Central Ry. Co.* v. *Iowa*, 160 U. S. 389 (1896).

The approval of the settlement by the Delaware courts is overwhelmingly supported by the record. The benefits flowing to the stockholders of Chrysler from the modified Incentive Compensation Plan are substantial, as indicated in the decision of the Supreme Court of Delaware (Pet. A21-24). One aspect of the modified Plan alone secures benefits to the stockholders that are huge. In this respect, actual figures for 1963 show that the stockholders' set-aside increased for that year under the new formula by $39,199,107 more than under the old formula on a before-tax basis and by $19,850,428 on an after-tax basis (A267-269; A279). Moreover, the new formula establishes a real task and a real incentive for the covered employees and at the

same time assures the stockholders that upon any payment under the Plan, they will have secured a substantial relative increase in their investment (A105-6; 132-3; 143; 156). In petitioner's brief to the Supreme Court of Delaware, at page 4, he significantly asserted that he "did not challenge the incentive compensation plan modification."

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari of the petitioner Arthur Hoffman should be denied.

Respectfully submitted,

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APPENDIX TO BRIEF OF GALLO RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI BY PETITIONER ARTHUR HOFFMAN

Decisions of the Court of Chancery of Delaware

SEITZ, Chancellor:

This is the decision after hearing on the fairness of a proposed settlement of two derivative actions.

The first action was commenced by one Sol A. Dann and other stockholders against Chrysler Corporation ("Chrysler"), various directors and officers as well as certain suppliers of Chrysler. This action will be referred to as the "Dann action".

The Dann action was commenced in August 1960, and involved some twelve causes of action. After certain pleading skirmishes (See Dann v. Chrysler Corp., Del. Ch., 166 A. 2d 431, 174 A. 2d 696), a consolidated amended complaint was filed consisting of some 109 pages embracing fifteen causes of action and about sixty separate claims. Certain of the defendants thereafter served their renewed motions to dismiss or in the alternative for a more definite statement. The so-called Keller defendants served their motion to dismiss or for summary judgment. The defendant John W. Minor and the defendant NAFI Corporation (the only appearing supplier) filed answers denying the charges asserted against them. The defendant Robert P. Laughna filed a motion to strike and to dismiss parts of the complaint.

All the motions to dismiss were based largely on the contention that the plaintiffs could not amend their complaint so as to assert new causes of action as to those non-resident defendants who had appeared generally following the sequestration of their property. Certain motions also questioned whether the allegations were set forth with

sufficient particularity. The Keller defendants raised the defense of statute of limitations.

In February 1962, Mary and James Gallo filed a derivative action against Chrysler and the then directors and certain past officers of Chrysler charging many of the same acts, omissions, and "frauds" as were alleged in the Dann complaint.

In June 1962, this court entered an order consolidating the Dann and Gallo actions solely for the purpose of discussing a possible settlement. The time fixed was subsequently extended at the request of the parties.

In the meantime (between 1960 and March 1963), four stockholder actions were commenced outside the State of Delaware embracing some of the same causes of action—two in the New York Supreme Court, one in the Federal District Court for the Southern District of New York and one in the Federal District Court for the Eastern District of Michigan. Also, Chrysler commenced a libel action against Dann in the Delaware Superior Court.

On March 6, 1963, a stipulation of settlement was filed. To facilitate the settlement a final amendment was filed by the Dann plaintiffs adding two additional causes of action which, it is suggested, incorporate the additional charges found in the New York and Michigan actions. The stipulation of settlement provides, inter alia, that all the derivative actions shall be dismissed with prejudice against all the defendants except the defendant W. C. Newberg. As to Newberg the dismissal will be without prejudice. Such fees and disbursements as the court may allow to plaintiffs shall be paid by Chrysler.

Under the terms of the stipulation of settlement, if approved, each of the individual defendants who is a party to the stipulation and all past or present directors of Chrysler, except the defendant Newberg, will receive a

release discharging each of them from any and all claims arising out of the matters alleged in the complaint and all amendments thereto both in the actions brought in this court and the "companion" actions in the New York state and federal courts. Also, the individual defendants who are parties to the stipulation will seek indemnity for their attorneys' fees incurred in connection with these actions.

On March 6, 1963, a court-approved notice of hearing on the stipulation of settlement was mailed to all stockholders. A proxy statement was simultaneously transmitted to the stockholders proposing the adoption of a modification in Chrysler's incentive compensation plan. The following language is contained therein:

> "Since the modification of the formula for computing the total provision that may be made for incentive compensation awards is a principal term of settlement and is necessary if the settlement is to be put into effect, a vote in favor of amending the 1956 stockholders' resolution to change the incentive compensation formula will, in effect, be a vote in favor of the settlement."

At a special meeting of the stockholders held on April 16, 1963, out of a total of 9,083,502 shares outstanding and entitled to vote, 6,699,016 shares were voted in favor of and 144,240 against the proposed modification.

The court also appointed an amicus to report, inter alia on "What appear to be the issues relevant to the hearing on the proposed settlement and the proof which might be of assistance to the court." This elaborate and helpful report was filed and was made available to all interested parties before the hearing. In particular, it discussed and analyzed the evidence of record relevant to the various issues and suggested other areas which might need elaboration.

Several stockholders filed objections, and the matter was tried at some length. The objecting stockholders are identified collectively herein as "objectors", unless more particular identification is desirable.

This is the decision on the "fairness of the settlement" after hearing and elaborate briefing.

Before the specific issues are considered, a little background is in order. Chrysler, a Delaware corporation, employs directly or through its subsidiaries in the United States approximately 77,000 people. It manufactures and sells passenger automobiles and commercial cars and trucks both here and abroad. It is the third largest manufacturer of such vehicles in the United States. It also manufactures assorted products of some substance including defense materials.

I turn now to the terms of the settlement and their relationship to the causes asserted.

The "consideration" offered in exchange for the releases and dismissal of the causes of action is a modification of Chrysler's present incentive compensation plan for its employees. The details of the present plan and the proposed changes are discussed more fully later herein. The Dann plaintiffs' attorneys also urge that the changes in Chrysler's management personnel (referred to later herein as a "change in management") which occurred both prior to and during the pendency of these suits, are attributable to the activities of the plaintiffs or their attorneys. They contend that such changes effectuated one of the principal purposes of the litigation and that they provide in and of themselves a sufficient basis for approving the settlement.

The proponents agreed that the stipulation of settlement and the proposed modification of the present incentive compensation plan should not become operative until the modification was approved by Chrysler's board and by its stockholders and final approval of the settlement was

granted by this court. Final settlement was also conditioned upon dismissal of the lawsuit instituted by Dann in the Federal District Court in Michigan against Chrysler and the giving of mutual releases between Dann and Chrysler of claims and counterclaims involved in the libel action filed by Chrysler against Dann in the Superior Court in Delaware plus the payment of $20,000 and disbursements to Dann's separate counsel therein.

In the stipulation all the named defendants (except Newberg) deny liability under any of the causes of action but agree that the expense of further litigation and the probable expenditure of time on the part of Chrysler's employees, officers ,and directors make it desirable that the litigation be terminated without further proceedings. Plaintiffs state that the "significant and steady progress in all phases of Chrysler's operations under new management * * * with the estimated benefits which will flow to Chrysler and its stockholders by reason of the amendment to the Incentive Compensation Plan" can be considered an achievement of the objectives of the litigation. Thus, they state that they believe that settlement on the proposed terms is much to be preferred to continuation of the litigation and is in the best interests of Chrysler and its stockholders.

In the court-ordered notice of hearing which was sent to the stockholders, plaintiffs' attorneys made certain representations with respect to plaintiffs' ability to recover on the alleged causes of action. These causes of action were divided by them into three categories: "(1) charges that certain past and present directors and/or officers of Chrysler have been financially interested in Chrysler suppliers and have personally profited from transactions between Chrysler and suppliers; (2) charges of mismanagement by defendants as directors and officers of Chrysler during the years 1956 to 1961; and (3) charges relating to the Incentive Compensation and Stock Option plans of

Chrysler including allegations that they were not soundly devised and provided rewards out of proportion to the performance required to gain the rewards and should be appropriately revised."

Plaintiffs' attorneys further stated in the notice that while they felt that inquiry into the alleged instances of wrongdoing was warranted, they had concluded that the evidence gathered did not sustain the charges of personal interest and personal profits on the part of the defendants, except in a few instances discussed in the notice, and would not permit successful prosecution of the charges. Next, plaintiffs' attorneys acknowledged that the charges of mismanagement against the named defendants lay primarily in the area of business judgment and that the burden of proving culpability was too great to promise success in the prosecution of such charges.

Plaintiff's attorneys stated finally that they believed their complaint concerning the "fairness" of the incentive compensation plan was well grounded and that a revision in such plan in accordance with their suggestions should be made. The revision or modification negotiated by plaintiffs' attorneys with the directors of Chrysler is said to meet these "suggestions" in that no compensation may be awarded under the new plan until higher earnings are achieved by the corporation but a higher rate of participation is permitted once these higher levels of earnings are achieved. As to the stock option plan, plaintiffs' attorneys noted that the directors of Chrysler had already made certain changes therein.

The proponents of the settlement all contend that the agreed terms are fair and beneficial to Chrysler and ought to receive the approval of the court. The defendants, however, deny that the change in Chrysler's management and the "changes and improvements in Chrysler which have occurred subsequent to commencement of the activities of

plaintiffs'' are, as contended by plaintiffs' attorneys, attributable to the plaintiffs.

The objectors who have formally appeared herein take the position that the court should refuse to approve the proposed settlement on the ground that it is ''unfair'' to Chrysler's stockholders. The heart of their contention is that in practical effect Chrysler will receive nothing of tangible benefit as a result of the settlement, and indeed may be giving up a present advantage, while in return it will be required to deliver a release from all further liability to each of the named individual defendants except Newberg. Except for the objector Ezzes (and perhaps Koenigsberg as later considered), the objectors do not urge that there is in fact merit in any of the causes of action set forth in the amended complaints sufficient to permit a recovery thereon. Thus, they do not suggest that the ''consideration'' offered in return for the releases is ''inadequate''. Rather they contend that the proposed modification of the incentive compensation plan is merely a device agreed upon by the proponents by which the defendants may avoid what plaintiffs' attorneys are said virtually to concede are worthless claims. Thus, in the view of the objectors, the proposed settlement will have the effect, inter alia, of committing the corporation to a radical change in its incentive compensation arrangement, such change having resulted not from an untrammelled exercise of discretion on the part of the directors and stockholders but from the necessity of finding a basis for settling the lawsuit.

A further and separate objection they say is the fact that the proposed modification of the incentive compensation plan, if instituted, will result in the authorization of greater dollar payments to Chrysler's employees under such plan than are presently permitted. Thus, they contend, no ''benefit'' can assuredly be said to pass to Chrysler as a result of the proposed settlement beyond the termina-

tion of the existing lawsuits with the consequent elimination of expense and unfavorable publicity and an end to the distraction of Chrysler personnel from their corporate duties.

Parenthetically, defendants' attorneys meet these objections to the settlement head on. They of course agree that the claims are worthless, and they concede that the modification of the incentive compensation plan if approved will authorize larger payments to Chrysler executives, a number of whom are defendants herein, if the requisite earnings exist. They admit that Chrysler's directors were anxious to terminate the litigation in order to avoid further expense and embarrassment to the corporation and "were willing to consider any honorable and proper way to get these suits out of the way".

They contend, however, that as a practical matter the corporation has nothing to gain from a continuation of the litigation and that it faces the prospect of further losses in time, good will, and expense. They urge that the modified incentive compensation plan will be an improvement over the old plan, since net earnings will have to be higher before the beneficiaries become entitled to the same dollar amounts of compensation as they would have been under the existing plan.

The defendants consider immaterial the fact that a number of them will be in a position to receive a greater dollar amount of incentive compensation for the year 1963 under the proposed plan than under the old plan. This they say is the result of Chrysler's financial success in the 1963 fiscal year and merely fulfills the purpose of the modified plan to give greater rewards for greater corporate success. They emphasize the fact that the stockholders as well as the directors approved the modification after being explicitly informed that approval was a vote in favor of the proposed settlement. Defendants' attorneys urge that even if there is doubt that the modified incentive com-

pensation plan is better than the old plan, still the court should approve the settlement since the interests of Chrysler can best be served by terminating the litigation.

Should the court approve the settlement on the basis of the terms agreed upon by the proponents and approved in effect by the holders of a vast majority of the stock by virtue of their affirmative vote on the modification of the existing incentive compensation plan?

I should note preliminarily that the objecter Ezzes charges that the 1963 proxy statement was tainted with fraud. This charge is based on the claim that the statement did not adequately or fully describe the nature of the claims and the effect of the proposed settlement. I find no merit to these charges.

Unlike the other objectors, Ezzes alone claims that there is in fact merit in many of the causes of action asserted in the Dann and Gallo complaints. He contends that the proposed settlement should not be approved by the court, because the consideration offered by the defendants in exchange for releases is wholly inadequate in view of the potential recovery by the corporation.

Before dealing with specific objections it would seem desirable to mention the record which is used as the basis for deciding this matter. The plaintiffs agreed to the terms of the settlement on the condition that they be permitted to have reasonable discovery so as to make a judgment as to whether the other claims had sufficient merit to negate the fairness of the proposed settlement. Rather elaborate discovery was undertaken. It resulted in the representation by plaintiffs in the notice to stockholders of the proposed settlement that except for the incentive compensation plan cause of action the other causes could not be successfully pursued. It is obvious, with all due regard for the integrity of counsel, that the approach taken is, at a minimum, subject to the possibility of real abuse. The court took this into consideration in passing upon

the objectors' requests for further discovery. In addition the court gave counsel for the various objectors an opportunity at the hearing to interrogate certain of the knowledgeable defendants and other witnesses whom the court required to appear for the purpose of testifying to a number of these matters. I have concluded that the record is sufficient for present purposes.

The objector Ezzes claims that a number of the causes of action have merit. He so contends with respect to alleged frauds on the part of Chrysler's management in administering Chrysler's incentive compensation plan. Strictly speaking, a number of these allegedly valid claims do not fall within the confines of the incentive compensation causes of action asserted in the Dann and Gallo complaints. The notice to the stockholders of the hearing on the settlement contains the following language:

> "In plaintiffs' discovery proceedings herein, the documents relating to the incentive compensation plan were marked as exhibits. In view of their examination into their charges against individual officers and employees of Chrysler, plaintiffs' attorneys have concluded that although there is an issue as to fairness of the existing plan, there was no invalidity in its adoption, or impropriety in the application of or calculations under the plan or any improper award of benefits thereunder except for any possible claim that Chrysler may have against Newberg. Pursuant to the stipulation of settlement of these actions, a modification of the plan as hereinafter more fully described, negotiated by plaintiffs' attorneys, will be submitted for stockholder approval."

I propose to resolve any doubt by treating each of the allegedly valid causes of action asserted by the objector as if they fell within the confines of the allegations of the

complaints. I note in passing that of all the claims originally asserted by the plaintiffs only the issue as to the "fairness" of the existing (1956) plan is said to have merit in connection with the defendants who join in the settlement proposal. I observe further that nowhere in the notice to stockholders or in plaintiffs' briefs is the precise nature of the alleged unfairness in the plan spelled out.

Three of the Ezzes objections are directed toward allegedly improper practices under the 1929 Chrysler incentive compensation plan and the allegedly fraudulent adoption of the 1956 plan.

The history of Chrysler's incentive compensation plan, commencing in 1929, forms the background for these contentions of the objector. On April 16, 1929, Chrysler stockholders authorized the payment of incentive compensation in the following language:

> "This corporation may incur obligations on account of such profit sharing plans and bonus plans, provided said expenditures for any calendar year * * * shall not exceed for said year six and one half percent (6½%) [1] of the *net earnings of the Corporation for that year* * * *." (Emphasis added)

Computation of incentive compensation for the period 1929 to 1955 was governed by the 1929 resolution set out above, which provides for the application of a percentage figure to the "net earnings of the Corporation". The proponents of the settlement concede that from 1929 to 1939 the "net earnings" against which the percentage was applied was a consolidation of the earnings of Chrysler and all wholly-owned subsidiaries, domestic, Canadian and foreign. From 1940 to 1953, however, Canadian and other foreign subsidiaries were not consolidated for incentive

[1] By resolution of the Board of Directors adopted February 23, 1941, this percentage was reduced to five per cent.

compensation purposes. Beginning in 1954, Canadian and foreign subsidiaries were once against consolidated. A comprehensive revision of existing incentive compensation plans was effected by the stockholders' resolution of April 17, 1956, which remains in force at the present time. The pertinent language of that resolution follows:

> "* * * this Corporation may incur obligations on account of Incentive Plans, provided the provision out of earnings for any fiscal year of the Corporation for all Incentive Plans then in effect * * * shall not exceed five per cent (5%) (as computed by the independent Auditors of the Corporation) of the *Consolidated Net Earnings for that fiscal year (as reported in the Annual Report to the stockholders) of the Corporation and such of its subsidiaries as are consolidated in its annual statements* * * *". (emphasis added)

The Ezzes objections on these matters are first that during the period 1929-1955, payments of incentive compensation were based on computations of consolidated net earnings when in fact they should have been based on the net earnings of Chrysler alone; next, that the 1956 stockholders' resolution relating to incentive compensation "changed" the basis for payments of such compensation to consolidated net earnings though the proxy statement failed to reveal that the 1929 formula did not permit consolidation; and finally, that during the period the 1929 formula was in force, the method of computation was improperly altered from time to time.

The defendants' answer to these objections is that the 1956 stockholders' resolution, as indicated in the proxy statement, merely restated the practices that had been adopted under the 1929 resolution and did not fundamentally change them although funded debt was added to

the capital base. Thus, the following statement is found in the 1956 proxy statement: "The proposed amendment generally revises the resolution of 1929 so as to eliminate what has become obsolete and to adapt the language to present-day accounting terminology". The defendants point out that the consolidation of wholly-owned subsidiaries for incentive compensation purposes, which is expressly authorized by the 1956 resolution, had always been Chrysler's practice though the 1929 formula only refers to "net earnings of the Corporation". Also, the earnings figures which have been used for incentive compensation purposes have been those shown in the annual reports to stockholders, though no reference is made in the 1929 resolution to annual reports of earnings.

The defendants say that foreign subsidiaries were not included in the consolidated financial statements in the annual reports to stockholders for the years 1940 through 1953, because of exchange restrictions and war-time conditions in foreign countries. They contend that this situation was explained to the stockholders in the annual report for the year 1940, although that report is not part of the hearing record. Thus, they urge that the practice of basing compensation on the financial statements appearing in the annual reports to stockholders was consistently followed throughout the period 1929 to 1955.

What assessment may be made of these supposed causes of action said to exist against some of the defendants herein? The court's responsibility at this stage is merely to evaluate the probability of success if these issues were ultimately litigated and not to make a final determination. Krinsky v. Helfand, 38 Del. Ch. 553, 156 A. 2d 90.

Turning then to the above contentions of the objector Ezzes, I am satisfied that the likelihood of success on any of these claims is very small. The defenses of laches or limitations might well be applicable to each of these claims. Moreover, assuming that Chrysler reported its earnings to

its stockholders on a consolidated basis prior to the institution of the 1929 plan, no valid objection could probably be raised to the interpretation of the language of the 1929 formula adopted by the persons charged with implementing such plan. A very similar situation is presented in Meyers v. Cowdin, Sup., 47 N. Y. S. 2d 471, where the New York court in dismissing the complaint after trial noted that the earnings of the corporation there involved had always been reported to the stockholders on a consolidated basis. It concluded therefore that payments of incentive compensation based on such consolidated earnings were not improper though the formula provided for payments based on "net earnings of the Company".

Next, I think that the objector's claim that the stockholders' resolution of 1956 was induced by fraud is without substance. It is conceded that incentive payments for the period 1929 to 1955 were based on the consolidated earnings of Chrysler and its wholly-owned subsidiaries as reported to the stockholders. It follows therefore that there was no misrepresentation or inadequate disclosure when the 1956 proxy statement stated that the purpose of the revision, which I find made no change of any real substance in the existing plan, was "to adapt the language to present-day accounting terminology".

Next, I turn to the objector's claim that the persons charged with implementing the plan improperly altered computation practices without regard for the language of the various stockholders' resolutions. I note first in evaluating this claim that there is no showing that the corporation or its stockholders were damaged by any of these alleged alterations.

The objector points principally to the exclusion of Chrysler's wholly-owned foreign subsidiaries from consolidated earnings during the period 1940 to 1953. The defendants claim, however, that the practice of excluding such subsidiaries and the reasons therefor were explained

to the stockholders in the 1940 annual report and that such information was filed with the S. E. C. I am satisfied that little success could be anticipated if this issue were litigated, since payments during this period were admittedly based on consolidated net earnings as reported in the annual reports to stockholders. There is no showing whatever that the alteration in the method of consolidation violated sound accounting principles, nor does the objector refute defendants' assertion that the allegedly improper alteration was fully disclosed to the stockholders.

The objector claims that there were other improper alterations in computation practices with respect to wholly-owned retail selling and leasing subsidiaries and so-called forfeitures. These claims appear to be wholly without merit. I merely note in passing, first, that the allegedly improper treatment accorded forfeitures served to reduce rather than increase the fund available for incentive compensation and, next, that the earnings of the selling and leasing subsidiaries were consolidated, in effect, with the earnings of the other subsidiaries in the annual reports to stockholders.

The objector Ezzes next complains that payments in 1955, 1957, 1960, and 1962 were improper because the language of the plan was misinterpreted so as to inflate the fund available for incentive compensation payments. The first matter under this head concerns the inclusion of state and local income taxes in 1962 as part of the fund from which "set aside" was deducted. The 1956 plan expressly permits the inclusion of "taxes on income". The objector contends, however, that the 1929 plan only permitted the inclusion of *federal* taxes on income and that the 1956 proxy statement implied the 1956 plan would continue on the same basis.

There are several reasons why in my opinion the probability of success on this issue is small. First, there is nothing in the 1956 proxy statement that can be said to consti-

tute a representation that the phrase "taxes on income" in the 1956 plan was to have the same meaning as "Federal taxes" in the 1929 plan. The most that may be said is that the amended language introduced a potential ambiguity in view of the former practice. Certainly this was an area where those in charge of implementing the plan were entitled to exercise their sound discretion. Also, I note that in November 1962, inquiry with respect to the proper interpretation of the language of the plan was directed to legal counsel by Chrysler's auditors. In reply, it was specifically stated that the language here in issue included state and local as well as federal income taxes. Thus, considering the factors relevant to the proper interpretation of this language, I think the likelihood of recovery from any of the defendants of the alleged overpayments for the year 1962 would be remote.

The objector next raises objection to the interpretations of certain portions of the plan which are found in the reply by legal counsel to Chrysler's auditors. I pause here merely to note that the objector disagrees with such interpretations. However, he does not point to any specific instance where payments were based on these allegedly erroneous interpretations of the plan. Thus, assuming that he were correct, there is nothing on which a recovery by the corporation could be based. I add, however, in order to avoid clouding this issue, that the interpretation placed on the language in issue by counsel seems fair and reasonable. I conclude therefore that prosecution of this claim would probably be fruitless.

The objector claims that the 1956 plan is invalid: (1) because incentive compensation can be based on non-operating income, (2) because loss years are not averaged with profitable years, (3) because the compensation percentage is applied to before-tax rather than after-tax earnings, and (4) because compensation is based on net earnings as reported to stockholders rather than net earn-

ings as reported to the federal government for tax purposes. I can only say that no authority is cited which suggests that any one of these reasons per se renders the incentive compensation plan invalid. At bottom, these objections are directed to the form of plan which the directors and stockholders voted to adopt. It may well be that some plan other than the one adopted would better accomplish the objectives of an incentive plan. But that of course is not for this court to say. I am satisfied that the contentions of the objector under this head offer no legal basis for attacking the 1956 plan.

The objector Ezzes also contends that all stock options issued after 1956 were invalidly issued in violation of the stockholders' resolution of April 17, 1956. I think it clear that the limitations placed in the resolution authorizing payments under "Incentive Plans" have no bearing on the issuance of stock options and that such options were not invalidly issued. While a stock option plan may indeed be considered an incentive plan, it is readily apparent that the term "Incentive Plans" appearing in the 1956 proxy statement and stockholders' resolution was not intended to and did not refer to the Chrysler Stock Option Plan.

Next, the objector claims that the cancellation of certain options in 1958 and 1959 and their reissuance at lower option prices constituted a waste of assets for which the recipients are liable. The 1959 proxy statement makes it clear that the granting of the new options, conditioned upon surrender of the old, was undertaken by the Stock Option Committee of Chrysler which was composed of directors not eligible to receive options. Each of these new options could be exercised by the holder only if he remained continuously in the employ of Chrysler or its subsidiaries for at least eighteen months after the date of its grant. The action of the Stock Option Committee was approved by the Board of Directors and by the stockholders.

The objector contends that the reissuance of stock options at lower prices constitutes a gift or waste of assets, since the committee action was taken only when it was made clear that there would be a net loss in earnings during 1958 thereby depriving certain of the defendants of incentive compensation for 1958. He also contends, citing certain magazine and law review articles, that the reissuance of stock options at lower prices ought not be permitted, since such action in effect excuses poor corporate performance.

A number of Delaware decisions I think support the view that where stock options are granted by a disinterested committee with the approval of the directors and stockholders and where the optionee is required to remain in the employ of the corporation for an extended period of time, no legal attack may successfully be made upon such options. See, e.g., Gottlieb v. Heyden Chemical Corporation, 33 Del. Ch. 177, 91 A. 2d 57; Beard v. Elster, (Del. Ch.). 160 A. 2d 731. One may have difficulty reconciling the practice of reissuing options at lower prices with the "incentive" aspect of the earlier grants. Nevertheless, the court would not be inclined to block reasonable corporate action in this area, particularly in view of the need of corporations to retain talented personnel.

I conclude therefore that the probability of success if this issue were ultimately litigated would under the circumstances be small.

The objector next attacks the "revolving credit agreement" negotiated by Chrysler with a number of banks whereby Chrysler was extended a credit commitment of $150,000,000. The commitment was obtained on June 12, 1958 and was continued until May 15, 1961. Although Chrysler never used the revolving credit, it nevertheless paid the sum of $2,157,553 to the participating banks during the period the commitment remained in effect.

The objector contends that six members of the nine-member Finance Committee that recommended the commitment were officers and directors of participating banks. All the members were present on June 12, 1958 when the matter was voted upon, and all voted except R. E. McNeill, Jr., President of the Hanover Bank, who had been the primary negotiator of the transaction. The Board of Directors of Chrysler voted upon the commitment at its meeting held the same day. Eighteen of the twenty-one directors were present. Of these eighteen, eight were associated with banks ultimately participating, and all voted except McNeill who nevertheless was present.

Article II, Section 9 of Chrysler's By-Laws provides that no director shall vote at a meeting of the Board on a question in which he is interested (with certain exceptions not relevant here) or be present while the same is being considered. Section 9 goes on to apply the same safeguards where a transaction between Chrysler and another corporation is involved and a director of Chrysler is a director or officer of such other corporation. The same limitation appears to be applicable to action taken by any committee of the corporation.

The objector contends that the presence of the interested directors at the meetings of the Finance Committee and the Board violated Section 9 of the By-Laws. He claims that by virtue of his position on the Stock Option Committee and Incentive Compensation Committee, McNeill had a "persuasive effect" on the other directors in obtaining their approval of the commitment. Next, he claims that Chrysler's undertaking was reckless and without diligence, since admittedly there were no studies on the subject of the revolving credit agreement before the Finance Committee or the Board at the time it was approved or while it remained in effect, though Chrysler never used the credit but continued paying for the availability of such credit. The objector seems to suggest that even if the initial credit

agreement in 1958 was warranted by the circumstances then prevailing, the subsequent improvement in Chrysler's Cash and Marketable Securities and Net Current Assets required reconsideration on the part of the Board. The objector attributes all these alleged wrongs resulting in payments by Chrysler of $2,157,533 over a three-year period to the conflict-of-interest situation in which certain of the directors found themselves.

The revolving credit agreement was the subject of the ninth Dann cause of action and the sixth Gallo cause of action. Much of the evidence relied upon by Ezzes in voicing his objection to the settlement of this claim was originally produced by the plaintiffs. In the notice to stockholders plaintiffs' attorneys summarized the claim and made the following statement:

> "Upon all the evidence plaintiffs' attorneys have concluded that the credit arrangement was fair and reasonable. Apart from the question whether a technical by-law violation might still be argued, plaintiffs' attorneys have concluded that these causes of action could not be sustained in the light of business considerations and the fact that there is no evidence that any director personally profited from the transaction."

In evaluating the prospects of success on this claim I assume without deciding that Section 9 of Chrysler's by-laws was violated by the fact that a number of "interested" directors were present and voted to approve the agreement. Does it follow that the directors involved are therefore liable for the amount expended by Chrysler for the availability of the credit? It is uncontradicted that Chrysler paid no more than the going rate for the commitment. Indeed, there is no "objective" evidence that the terms were unfair to Chrysler or that the participating directors were

guilty of bad faith. The thrust of the Ezzes objection is that the interlocking directors, because of their conflict of interest, recklessly committed Chrysler to a credit commitment which it did not really need. I am of the opinion, however, that the evidence of record on this matter fully supports the view, even on the assumption that the defendants must bear the burden of proof, that the commitment was reasonably necessary for the purpose that it was intended to serve and that the need therefor was reviewed periodically and reaffirmed. Considering the background and experience of the members of Chrysler's board as well as the other evidence, I do not think the absence of written studies is indicative of a lack of diligence on the part of the directors in approving the commitment or allowing it to continue. Thus, apart from the alleged by-law violation, I am satisfied that the defendants could successfully have vindicated their conduct.

What then is the legal effect of the violation of Section 9 of the By-Laws? Certainly such conduct gives just cause for apprehension, but it does not follow in my opinion that the defendants are therefore absolutely liable for the dollar amounts paid by Chrysler for the commitment. None of the defendant directors received any personal profit from the transaction, nor did Chrysler receive less than its "money's worth". It follows therefore that any sum these defendants are required to pay to Chrysler will be in the nature of punitive, as opposed to compensatory, damages.

There are instances where the court will impose such damages in order to vindicate a legislative or other public policy. Generally speaking, however, in the absence of fraud or bad faith, a court will not upset a transaction involving corporations having even a majority of directors in common where the transaction is shown to be fair. In the present case, less than a majority of the directors were associated with banks ultimately participating, and one

cannot fairly say that undue influence was exerted as to the rest. I recognize that the utmost vigilance is required in a case such as this, but where a close scrutiny of the record fails to disclose any meaningful evidence of actual wrongdoing or damage to the corporation, the monetary worth of the claim is most dubious. I conclude from the foregoing that plaintiffs' attorneys were justified in stating that these causes of action could not be sustained.

I turn next to the objector's claim that the directors of Chrysler acted recklessly in purchasing a substantial minority interest in Simca prior to 1963. The objector does not contend that there was any conflict of interest involved in this transaction. Thus, in substance he is attacking a decision involving a business judgment on the part of the directors. I am satisfied from the record before the court that the evidence adduced in support of such claim is wholly inadequate to afford any hope of meeting the heavy legal burden imposed in this area.

Both Koenigsberg and Ezzes object to the proposed settlement with the defendant NAFI Corporation. NAFI was charged in the Dann complaint with having sold inferior textile materials to Chrysler at excessive prices and in greater quantities than were needed. The defendants K. T. Keller, Samuel Keller, and L. L. Colbert allegedly were "financially interested in and involved with NAFI Corporation" and caused Chrysler to make such purchases. NAFI denied the charges though it admitted that K. T. Keller had owned varying quantities of its common stock.

NAFI is not a defendant in the Gallo action though the charges are repeated in substance in the Gallo complaint.

Under the terms of the proposed settlement the claim against NAFI will be dismissed with prejudice. NAFI will not be required to pay a consideration in any form to Chrysler. No release will be given to NAFI.

The record shows that the stock owned by K. T. Keller in NAFI never exceeded 1.05% of the outstanding common stock of the corporation. Apart from that, the record is devoid of any evidence of wrongdoing on the part of this defendant in support of the alleged claims. The objector Ezzes charges that "the proponents willfully refrained from developing evidence sufficient to enable a proper evaluation of the NAFI cause of action." I am satisfied that the charge of "wilifulness" on the part of the proponents is wholly unfounded and that the evidence adduced by the plaintiffs warranted their representation that they could not succeed in establishing that Chrysler had suffered any damages. Ezzes suggests an area where further evidence might have been sought by plaintiffs with respect to this cause of action. There is no showing by the objector, however, that any of this evidence if produced would have added substance to the alleged claim.

Next, the objector Koenigsberg seems merely to suggest that since NAFI is giving no consideration to Chrysler, the settlement should not be approved as to it. In view of the fact that both the plaintiffs and Chrysler agreed that the charges are unfounded and the record does not indicate anything to the contrary, I will approve the proposed dismissal as to this defendant if the general settlement is approved.

Ezzes also claims that the plaintiffs wilfully failed to produce evidence in support of the claims involving the so-called Consolidated Coal and National Steel transactions. Plaintiffs' attorneys represented in the notice that they had no evidence of any improprieties in these transtions. In my opinion such representations are fully supported by the extensive record on these matters. The objector says that further evidence should have been sought, but here, as in the NAFI transaction, there is no showing that the additional proof would add substance

to these claims. This is particularly true because of the evidence adduced before the Court.

The claims by the objector Ezzes that the salaries paid to Colbert and K. T. Keller constitute "gifts" are without substance. There is no evidence of wrongdoing in the negotiation of either of these contracts, and the "proof" tendered in support of the charges of breach of contract offers meager hope of ultimate success on these claims.

One other claim needs mention here. The objector Koenigsberg urges that the claims against the defendants Minor and Colbert with regard to the so-called Taxi-Ad transaction should be dismissed without prejudice and that neither defendant should receive a release or be reimbursed for his expenses by Chrysler. The objector does not contend that a real promise of success exists with respect to these claims. He states only that since neither defendant is presently an officer or director of Chrysler, neither can be said to have offered anything to Chrysler for settlement. He contends, however, that a "prima facie case" exists against Colbert.

After reviewing the evidence on this matter, I am satisfied, in view of Minor's relatively insignificant role in Chrysler's affairs and the disclosures involved, that no reason presently exists for not disposing of this claim as part of the general settlement.

Having weighed the claims asserted by the objector Ezzes to have merit and the possible defenses, I conclude that the probability of success in litigating any of such claims is so remote as to entitle them to practically no consideration in evaluating the fairness of the terms of settlement. I turn then to the claims asserted by the plaintiffs herein. The only claim which the plaintiffs now contend has merit is that which relates to incentive compensation. Let us examine this claim.

The tenth Dann cause of action and the eighth Gallo cause of action as finally amended stated several "claims"

relating to the present incentive compensation plan which was adopted by Chrysler's board and stockholders in 1956. These complaints alleged that the adoption of the plan was invalid and that the payments which were permitted thereunder were excessive and unconscionable. The formula was said to be improper because incentive compensation was permitted to be paid before the shareholders had obtained a reasonable return on their invested capital and because loss years were not set off against years in which there were profits in determining the availability of incentive compensation. Furthermore, plaintiffs claimed generally that payments had been inflated by miscalculations in applying the formula and by changes in accounting practices and policies. Finally, plaintiffs urged that at a matter of law officers found to be guilty of breaches of fiduciary duty to the corporation were not entitled to receive any incentive compensation whatever.

In the stipulation of settlement plaintiffs' attorneys represented that they had investigated the various claims under these causes of action and had reached the conclusion that the only issue that might profitably be pursued concerned the "fairness" of the existing plan. In attempting to evaluate the substantiality of this claim, however, one is met at the outset by the fact that plaintiffs or their attorneys have not further delineated the nature of the alleged "unfairness" purportedly found by them in the present plan.

Let us examine the present incentive compensation plan, plaintiffs' claims with respect thereto which might reasonably raise an issue as to "fairness", and the proposed modification of such plan.

Under the existing (1956) formula, incentive compensation awards may be made only for those years when consolidated net earnings of the corporation and consolidated subsidiaries (as reported in the annual report to the stockholders) *before* taxes on income and before provision for

incentive compensation and interest on long-term debt of the corporation, exceed 7% of the shareholders' investment (capital, surplus and retained earnings) in the corporation and consolidated subsidiaries and long-term debt of the corporation. The total provision for awards in any year is limited to 5% of such excess. The 1956 formula does not contain any provision limiting the bonus fund in any year to the amount of dividends declared in such year, or any other dividend limitation.

The only issue as to the "fairness" of this plan which might reasonably be said to have been raised in the Dann complaint and which has not been conceded by the plaintiffs to be without merit is the claim that the present plan is wasteful, because it permits payments to be made in excess of what could be granted under the comparable incentive compensation plans of Chrysler's principal competitors. The Dann complaint asserts that the plan should permit payments only when the income of the corporation exceeds a reasonable return on the stockholders' investment, the present Chrysler plan requiring a "set aside" only of 7% of the stockholders' investment before taxes, which is the equivalent of about 3½% after taxes. Such payments are said to have been particularly wrongful under the circumstances, because Chrysler's position in the automotive industry has declined since 1956 while the incentive payments to Chrysler employees during that period have nonetheless been substantial. A similar charge was made in the Gallo complaint.

It can be fairly said I think that, generally speaking, both the Dann and Gallo complaints challenge the set-aside percentage in the present plan as "unfair" on the ground that the return on the stockholders' investment is too small in relation to the amount of incentive compensation that can be awarded. In this sense "an issue as to the fairness of the existing plan", as stated by the proponents in the stipulation of settlement, can be said

to remain in the case. This disposes of a suggested objection to the settlement that it is not "related" to any of the causes of action. Compare Manacher v. Reynolds Metals (Del. Ch.), 165 A. 2d 741. I pass over for the time being the problem of evaluating the probability of success on the plaintiffs' part if ultimately they were to litigate this issue.

The proposed plan, as modified in accordance with the terms of the settlement, provides that for the years 1963 through 1969, incentive compensation awards may be made only for those years when the sum of (1) consolidated net earnings of the corporation and consolidated subsidiaries (as reported in the annual report to the stockholders) *after* taxes on income, and (2) provision for incentive compensation, and (3) interest on long-term debt of the corporation, exceeds 5½% of the stockholders' investment (capital, surplus and retained earnings) in the corporation and consolidated subsidiaries and long-term debt of the corporation. The total provision for awards in any year is limited to the lesser of 12% of such excess or the aggregate amount of all dividends declared upon the common stock of the corporation during the year.

The basic changes brought about by the modification have been the conversion of what was previously a before-tax incentive plan into an after-tax plan, an increase[2] in the set-aside (i.e., the return on the stockholders' investment before payment of any incentive compensation under

[2] The 7% stockholders set-aside under the 1956 formula relates to before-tax earnings, whereas the 5½% stockholders' set-aside under the 1963 formula relates to after-tax earnings. Consequently, assuming a 50% effective tax rate, on an after-tax basis the 7% set-aside under the 1956 formula would be equivalent to only 3½%, as compared with the 5½% set-aside under the 1963 formula. Conversely, on a before-tax basis, the 5½% set-aside under the 1963 formula would be equivalent to 11%, as compared with 7% under the 1956 formula.

the plan), and an increase [3] in the percentage of compensation to be awarded after deduction of the set-aside.

Thus, the 1963 formula requires a higher level of earnings before any award of incentive compensation may be made, by reason of the higher set-aside. Until the "cross-over point" is reached (i.e., the point at a still higher level of earnings where the amount of the bonus fund would be the same under both formulas), the higher set-aside under the 1963 formula would more than offset the higher rate of bonus so that a smaller bonus fund would be created under the new formula than under the 1956 formula. But once the level of earnings rises above the cross-over point a larger bonus fund will result under the 1963 formula than under the 1956 formula. However, under the 1963 formula, as a result of the increase in retained earnings, the set-aside in each succeeding year becomes greater than it would have been under the 1956 formula thereby requiring an even better earnings performance in each of these years to obtain the same bonus fund.[4]

To a certain extent then plaintiffs can fairly claim that they have achieved at least one of the objectives of their suit which was to increase the set aside and thereby increase the amount of income which must be earned by the corporation before equivalent amounts of incentive

[3] The bonus rate of 5% under the 1956 formula relates to before-tax earnings whereas the bonus rate of 12% under the 1963 formula relates to after-tax earnings. Assuming a 50% effective tax rate, on an after-tax basis, the 5% bonus rate under the 1956 formula would be equivalent to 10%, as compared with the 12% bonus rate under the 1963 formula. Conversely, on a before-tax basis, the 12% bonus rate under the 1963 formula would be equivalent to 6% as compared with 5% under the 1956 formula.

[4] The amicus computed that for the ten-year period 1953 through 1962, the total bonus fund would have been $3,748,713 less than it was, had the 1963 formula been applied.

compensation can be paid. That is not to say of course that plaintiffs' claim as to "unfairness" in the present plan is well founded. Indeed, considering the facts of record now before the court, I think the probability was small that ultimate success could have been achieved on this issue. Because of this, however, the plaintiffs, defendants, and objectors have taken radically different approaches in attempting to sustain or attack the validity of the proposed settlement.

The plaintiffs vigorously urge that the proposed modification plus the changes in management, etc., which were mentioned before, are "beneficial" to Chrysler and accomplish the objectives of the lawsuit. Thus, the plaintiffs have attempted to formulate the settlement within the traditional framework of a quid pro quo offered by the defendants in exchange for releases from further liability.

The defendants, including Chrysler, ignore the traditional approach. They deny there is merit to any of the claims, and while they believe that the modified plan will be advantageous to Chrysler and its stockholders, they do not believe that it remedies any supposed defect in the old plan. They agree that apart from the settlement, Chrysler's management had not previously given any consideration to a modification of the existing bonus plan.

The defendant urge that regardless of the extent to which the modification can be said to "benefit" Chrysler, the court should approve the settlement as fair and reasonable, since the expense of continuing the litigations will far outstrip any potential recovery.

The objectors, except Ezzes,[5] agree with the defendants that all the claims are without merit and should be

[5] The Ezzes objections are considered above and have been rejected by the court. Ezzes, however, also joins in the objections here stated, viz., that the proposed modification is not a proper or adequate consideration for settling the lawsuit.

disposed of. They disagree, however, that the lawsuit may properly be settled on the basis proposed by the plaintiffs and defendants. The objectors' contentions are basically reducible to two propositions. First, it is said, the proposed modification offers no demonstrable benefit of any kind to Chrysler though, if approved, it will commit Chrysler to a substantial change in its compensation plan. Secondly, as a practical matter, approval of the modification by the court will create for Chrysler's employees, a number of whom are defendants herein, a larger fund for the year 1963 than would be available under the existing plan. The objectors say that reasonably viewed, the defendants must have been aware of such fact when they agreed to the settlement.

The objectors suggest that plaintiffs' attorneys supported the proposed modification as part of the settlement not because it would remedy some arguable defect in the existing compensation plan, but because it would give color to their claim for an allowance of attorneys' fees. The defendants were willing to accept these terms, it is said, because they were required to surrender nothing in return for their releases. Moreover, since Chrysler's earnings for the fiscal year ending in 1963 promise to exceed the "cross-over point", the bonus fund will be larger than if the 1956 formula were still in effect. For all these reasons the objectors urge that the proposed settlement be rejected as unfair and unreasonable.

Having considered the nature of the claims and the possible defenses, I agree with the basic position of the defendants and objectors that there is little, if anything, to the causes of action asserted by the plaintiffs. Obviously in such a case settlement of the litigation is in the best interest of the corporation and in fact is much to be desired from the point of view of all the interested parties. The problem I am confronted with here, however, with due regard for the court's obligation to exercise its judg-

ment with respect to the fairness of the settlement, lies in determining what terms may properly be accepted by the court.

Common sense it seems to me would dictate that where the hope of recovery on the part of the plaintiffs, and thus on the part of the corporation, is small, little can be demanded from the defendants by way of settlement. Certainly this is the case here.

The objectors say, however, that no settlement can be approved unless there is technical legal merit to the claims asserted in the complaint and consideration of some formal nature is offered by the defendants in exchange for their releases. Thus, they urge that if the complaints lack legal merit, they should be dismissed with prejudice. They should not be permitted to become the basis for a supposed settlement wherein the defendants offer nothing because the claims asserted against them have virtually no value.

Assuming without deciding that the rule urged by the objectors might be applicable in a case where the court could say with complete confidence that the claims lack "technical legal merit", nonetheless it is clear that this is not such a case. There is no doubt that in the technical sense many of the asserted claims would survive a motion to dismiss, assuming the defendants chose to press such a motion. Thus, if the court were to reject the proposed settlement, the parties would merely be in the position of having to continue the litigation. It is just this situation which, with some justification on either side, both plaintiffs and defendants hope to avoid. Under the circumstances, I think that the court need only determine whether the terms are fair when measured against the probability of recovery on the asserted claims.

The objectors next contend, however, for a wide variety of reasons, that the court ought not accept a modification of the incentive compensation plan as the basis for settlement. First, apart from the fact that the modified plan is

likely to give the individual defendants a greater return than the old plan for the year 1963, the objectors contend that the proposed plan cannot be shown to be an improvement over the old plan and therefore is not a "valuable consideration" offered by the defendants for settlement. The basis for this contention is that no one can adequately foresee what the future holds for Chrysler in the way of profits. The objectors purport to show that it is probable that Chrysler will operate in the future at or above the cross-over point and therefore that the payments to Chrysler employees will probably exceed what they would have been under the old plan. This conclusion, however, rests on the selective use of available financial data with which in my opinion one may either agree or disagree. The objectors say, however, that in any case the modification must be rejected because the proponents have the burden of showing that the modification will result in smaller incentive payments or otherwise provide some demonstrable benefit to the corporation and this they cannot do.

It is fair to say I think that no one can predict with certainty what degree of success Chrysler will have in its operations in future years. Although Chrysler enjoyed a series of profitable years from 1950 to 1957, it showed a loss in 1958 and 1959. No one will deny, moreover, that the earnings of a major business corporation engaged in the production of automobiles are subject to a number of variables, some of which have little, if any, relationship to the amount of effort exerted by management. To that extent of course the objectors are justified in asserting that the proponents cannot "prove" that incentive payments will be smaller in any particular year in the future. All that may be said in the final analysis is that under the preposed modification earnings will have to be higher, up to the cross-over point, in order for payments to be the same as they would have been under the old plan but once that point is exceeded, payments can be larger.

Does the fact that there is no assurance that the fund and thus the probable payments in any particular year will be smaller under the proposed formula than under the existing formula vitiate the modification of the incentive compensation plan as the basis for settlement? Clearly there are dangers involved in this type of settlement where the only "consideration" offered by the defendants is the taking of some corporate action which not only involves no immediate detriment to the "charged" defendants or "assured" benefit to the corporation but also may in fact ultimately result in larger compensation payments to the defendants, among others. That is only to say, however, that each such case must be considered on its own merits. The objection made is not so much that the defendants are not giving a sufficient "consideration" but that they are purporting to give a consideration when in fact they are giving no consideration at all. The objectors state that they would prefer the actions to be dismissed rather than settled on the proposed basis. Since a refusal to approve the settlement cannot be equated with a dismissal of the actions, the objection here seems clearly to be related to plaintiffs' claims for an allowance of attorneys' fees rather than opposition to the termination of the pending litigations.

I am satisfied that as a practical matter settlement on the basis of the proposed modification is fair and reasonable subject to the limitation hereinafter imposed. Rejection of the settlement generally would clearly not be in the interest of Chrysler or its stockholders. While, as I have indicated before, there can be substantial disagreement as to whether the proposed change in the incentive compensation plan is an "improvement", there is no substantial showing that it will be detrimental to Chrysler. To the extent that this issue may be said to be poised in the balance, I think that the overwhelming approval of the modification by Chrysler stockholders with the knowledge that they were

in effect approving the settlement constitutes a "plus" for the approval of the settlement.

Because much is made of it, I next consider the additional contention of the Dann plaintiffs that the "change" in Chrysler's management which has presumably occurred is itself sufficient consideration for settlement of the lawsuits. The Dann plaintiffs charged in their complaint that certain directors, officers, and employees of Chrysler were guilty of gross mismanagement, and they sought, inter alia, the appointment of a receiver for Chrysler. The Dann plaintiffs contend that a major objective of this litigation has been to effect a change in Chrysler's management. They claim that the present lawsuit coupled with Dann's earlier activities is substantially responsible for such change or changes as have occurred in Chrysler's management.

Assuming without deciding that Dann's activities both before and after the filing of the complaint produced what he now describes as a "change in management", how, one asks, does that fact bear on the issue as to the fairness of the proposed settlement?

The defendants deny that any changes or improvements in Chrysler which may have occurred since the commencement of the plaintiffs' activities are attributable to the plaintiffs. It is certain, in any event, that the so-called change of management is not a "benefit" tendered to Chrysler by the defendants as a term of the settlement.

As I view the matter, it makes little difference on the issue as to the fairness of the settlement whether plaintiffs are credited with the presumed change in management or whether such changes are in fact beneficial to Chrysler. The paramount factor, as was noted before at some length, is that Chrysler and its stockholders have little to gain from a continuation of these litigations. Even if I were to conclude that these changes of personnel are not attributable to the plaintiffs, it could hardly be urged that the

court should therefore withhold its approval of the settlement.

The objectors offer certain other reasons why the settlement on the proposed basis should be rejected. First, they say that modification of the incentive compensation plan could have been undertaken by the directors and stockholders apart from settlement if the modification were thought worthwhile. This is of course true, but it does not follow that the old plan was improper. Indeed, the record would support a contrary conclusion. This being so the new plan and tender thereof as a basis for settlement cannot be evaluated as merely the result of their having performed their duty.

The objectors next say, however, that stockholder approval should be disregarded here because the stockholders may have felt that the modified plan should be adopted not because it is meritorious in and of itself, but because it was in the interest of the corporation to terminate the litigations. Assuming that the psychological motivation of the stockholders was as the objectors suggest, nonetheless I do not think their objection is of decisive significance. After all the most that may be said is that the stockholders were called upon to make a business judgment weighing the desirability of continuing the litigations against the supposed merits of the modified plan. Their approval is at least some evidence that the terms of the proposed settlement are fair. To this may be added the fact that the raising of the so-called cross-over point should certainly in the long run result in an increase in the stockholders' equity.

Finally a point is made that the tendered plan is incompatible with the legal principle found in Nadler v. Bethlehem Steel Corp., 38 Del. Ch. 427, 154 A. 2d 146, and Duane v. Menzies, 37 Del. Ch. 416, 144 A. 2d 229 to the effect that the tendered terms of settlement must be sufficiently definite

and beneficial to be capable of present valuation at least in a comparative sense. First of all, the approval of this settlement will not constitute a judicial imprimatur of its future operation. Indeed, the court in the Nadler case later approved a settlement after it was made clear that its future operation was not being approved. While it is true that there is no assurance that during the "term" of this plan there will be a monetary "saving" to the corporation, the fact is that business-wise it should benefit the corporation. Therefore, considering its inherent limitations and the limited qualifications hereinafter imposed, I do not believe that the Plan runs afoul of either the Nadler or the Menzies cases.

I therefore conclude that in the application of the governing standards this settlement should be approved with one qualification. It is clear that the directors "bargained" for this settlement in the context of a profit picture for Chrysler that practically assured the directors that the "new" plan would produce a substantially greater fund than would the old plan for 1963. Thus, even with due allowance for the fact that the future operation under the plan is an "unknown", I do not believe that it is appropriate for the director defendants who are beneficiaries under the plan to receive the fruits of the new plan for 1963. I will therefore approve the terms of settlement on the condition that the director defendants who are beneficiaries under the plan agree that as to the year 1963 they will derive no added financial reward solely as a result of the modification. If they so agree I will expect counsel to suggest mechanics by which such a result can be achieved. If counsel cannot agree they may submit suggested alternatives by a fixed date.

One further matter of substance requires attention. Under a separate arrangement Chrysler has agreed, if the present settlement is approved, to pay a $20,000 fee to

Dann's attorney in the libel action in the Superior Court. The Sandler objectors say that this payment is an "improper preference" to Dann over other stockholders and therefore should be disapproved by the court.

The testimony disclosed that at least some of the $20,000 payment is justified by Chrysler on the basis that it represents, in part, payment for legal services rendered the Dann plaintiffs in this litigation by the attorney involved. The balance is presumably justified on the basis of a business-judgment settlement by Chrysler of the libel action which was complicated for Chrysler by a contemplated counterclaim by Dann for damages based on alleged abuse of process.

Preliminarily, the court is not asked to "approve" the $20,000 payment. Thus, contrary to the request of the Sandler objectors, it cannot "disapprove" the payment as such. As a practical matter, all the court can do at this stage is disapprove the entire settlement on the ground that the intended payment renders the entire settlement unfair. I note, however, that the Sandler objectors do not urge that the settlement be disapproved on this score. They merely ask that the court not permit this payment.

In discharging my duty here, I have considered this dubious fee arrangement a negative factor in arriving at my judgment concerning the fairness of the terms of settlement. However, I do not consider it a sufficient basis for refusing such approval. If I felt that the payment were a sham or device to provide an out of court "pay-off" to obtain a settlement which ignored the interest of the stockholders generally, I would not hesitate to withhold approval of the settlement. The record, however, does not warrant such a conclusion. Moreover, the Gallo plaintiffs and their attorneys, who helped negotiate this settlement, did not participate in any of the negotiations surrounding the disposition of the libel action. Thus, I do not think the fairness of the

settlement herein is in fact impugned by the agreement to pay a fee to Dann's separate counsel.

However, I think it apparent that the payment of the $20,000 fee is, euphemistically speaking, intimately connected with the settlement of the derivative actions. Thus, to the extent that any of the intended fee represents payment for services allegedly rendered in connection with those actions, the effect of the arrangement would be to circumvent the powers generally exercised by this court in supervising such payments.

Thus, while the settlement itself ought not be disapproved as "unfair" because of the proposed payment, I am of the opinion that disposition of this fee matter should await the hearing on the question of plaintiffs' fees generally. Perhaps Dann and Chrysler will agree that payment of the stipulated sum or any part thereof will abide a decision by this court as to its propriety when judged by controlling Chancery standards. If not, then the matter will be considered in determining whether and to what extent Dann is entitled to reimbursement for counsel fees herein.

Other assorted matters not herein mentioned have been considered. They have been determined either to be consistent with the conclusions herein reached or irrelevant thereto.

Present order on notice.

ON MOTIONS FOR REARGUMENT

Motions for reargument have been filed by the Ezzes, Koenigsberg, and Sandler objectors. They say the settlement should be approved only on the condition that the new incentive compensation plan take effect as to all beneficiaries on January 1, 1964 rather than January 1, 1963, as provided in the proposed settlement. The basis for their

contention is found in this court's prior opinion. There the court said that the settlement would be approved on the condition that the director defendants who are beneficiaries under the plan agree that as to 1963 they will receive no additional financial reward solely as a result of the modification. This was done because it was found "that the directors 'bargained' for this settlement in the context of a profit picture for Chrysler that practically assured the directors that the 'new' plan would produce a substantially greater fund than would the old plan for 1963".

The objectors in effect say that there is no reason why any beneficiaries of the plan, not merely the director defendants, should benefit in 1963 when the financial picture for that year was as indicated, particularly since the new plan was tendered as a settlement device. In their answer to the objectors' motion, certain defendants say that the court erred in finding that the directors bargained for this settlement in the context above quoted. Thus, they say the condition was imposed on the basis of an erroneous premise and it would therefore be compounding the error to extend the condition to all the beneficiaries of the plan. They say that only one director participated in the negotiations and that he largely settled the terms as early as February 1962.

The problem under consideration must be evaluated in the light of the function the court was called upon to perform, viz., to pass upon the fairness of the settlement. Parenthetically, when the court was writing the original opinion, it considered the possibility of imposing the condition now suggested by the objectors.

Because the changed incentive compensation plan, rather than any "consideration" flowing from the real defendants, was tendered as the basis for the settlement, the court felt compelled to evaluate carefully the result of the change particularly insofar as the director defendants were concerned. It was reasonably clear to me from the record that there had been general public acceptance of Chrysler's cars

for the model year 1963. This was evident not only from the earnings picture for the last quarter of 1962 but from the figures for most of the first quarter of 1963. These matters plus the general financial prospects for Chrysler were of course known when Chrysler agreed to the settlement in final form in late February 1963 and again when the board confirmed the settlement in late March 1963. The knowledge and expectations of the defendant directors concerning Chrysler obviously put them in the position where they at least for the year 1963 could obtain a complete release from the litigation not only without paying anything personally but by finally approving a revised plan which would probably assure them even greater compensation payments for 1963.

In my prior opinion I used "bargained" in relation to the time the matter ripened for judicial consideration. Perhaps "bargained" was an unhappy choice of language. It might have been better to say "finalized". In any event the settlement cannot be justified by the directors by refusing to consider what the true situation was when the matter was finally ripe for submission to the court. They had a continuing duty to the stockholders to agree only to what was then fair.

I also note that the defendants' answer to the motion emphasizes that the new plan was negotiated by one director and that the director defendants subject to the condition constitute a minority of the entire board of directors. From these facts they seem to be suggesting that the imposition of the condition is either unfair or is based on actions which were not under their control. I need not consider the legal niceties of this problem in the context of mere adversary proceedings. As noted, the directors approved a settlement in the light of a profit picture which resulted in benefits to certain members of the board. Minority or not, the result was reasonably certain to provide some of its members who were defendants with a benefit

at least for 1963 which was greater than they would have received had the lawsuits been litigated and decided in their favor. In the face of the total picture presented, particularly in view of defendants' evaluation of the merits of the lawsuits, this was a benefit which I felt in fairness should be removed.

Thus, the court does not feel that the premise in the prior opinion for imposing the condition upon the director defendants is unwarranted. Nevertheless, this does not aid the objectors here because the non-director beneficiaries of the plan were not personally involved in approving the change and making it applicable to 1963. Also, not being defendants, they were not receiving any benefit for the release of corporate causes of action against them. Moreover, in the long view of this plan one cannot say with objective assurance whether it will or will not be more beneficial to the participants. Ineed, it may be less so. Thus, the court adheres to the limited condition imposed in the prior opinion.

The Sandler objectors also argue that the court should adopt the January 1, 1964 date generally, because it now knows the effect of the new plan for the year 1963. Passing over the element of hindsight, I believe this point overlooks the fact, noted above, that we are dealing with a seven year plan. The fairness test cannot be applied by looking at the results of only one year. The imposition of the condition on the defendant directors was imposed for reasons special to them.

Other grounds for reargument either are adequately treated in the prior opinion or do not call for any change therein. Thus, the motions for reargument are denied.

Present order on notice.

Post-Hearing Brief of Objector Arthur Hoffman to the Court of Chancery

The objector Hoffman, at this time, will merely make certain observations based upon the evidence adduced at the hearings upon the objections.

Firstly, it is respectfully pointed out that the amount of legal fees to be paid to the attorneys representing the individual defendants, which amount was revealed at the hearing, are totally excessive in view of the fact that Chrysler's attorneys were carrying most of the defense of this litigation. Further. the evidence at the hearing clearly showed that there was a substantial basis for the plaintiffs' claims of mismanagement at Chrysler. Therefore, to saddle the stockholders of Chrysler with attorneys' fees for services rendered for the benefit of officers and directors who condoned mismanagement would appear to be unconscionable.

In addition to the above the evidence at the hearing clearly showed actionable mismanagement on the part of Chrysler and to permit the officers and directors of this firm to get off scot free would appear to be unwarranted.

The undersigned requests the indulgence of the Court with respect to the law involved which will be set forth in detail at the time that Reply Briefs are due.

Dated: June 26, 1963

Respectfully submitted,

ARTHUR HOFFMAN, Objector
12 Landau Avenue
Elmont, New York

Motion of Objector Arthur Hoffman to the Court of Chancery to Stay Proceedings, to Take Depositions, and for Intervention

Arthur Hoffman, an objectant herein, hereby moves for a stay of proceedings for ninety (90) days in connection with the proposed settlement of the above-entitled actions and pursuant to Rules 26 and 34 to take the depositions of Sol A. Dann, Chrysler Corporation by its appropriate officer, NAFI Corporation by its appropriate officer, the corporate defendants named in the Complaints herein by their appropriate officers, and the individual defendants named in the Complaints herein, and to direct the parties, whose depositions are to be taken, to produce all relevant books, records, documents and tangible things relating to the issues involved herein and to permit the said objectant Arthur Hoffman to intervene in the above-entitled actions as a party plaintiff.

The grounds supporting the relief requested are set forth in the accompanying affidavit of Arthur Hoffman which is made a part of this Motion.

Dated: February 21, 1964.

Yours, etc.,

SOTIERE S. KAPSALIS,
Attorney for Objector,
Arthur Hoffman,
1001 Bank of Delaware Building,
Wilmington, Delaware.

I. WALTON BADER,
Attorney for Objector,
Arthur Hoffman,
170 Broadway,
New York, New York 10038

Affidavit in Support of Foregoing Motion

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

ARTHUR HOFFMAN, being duly sworn, deposes and says:

I am a present stockholder in Chrysler Corporation and own twenty (20) shares of the common stock of that company. I am a stockholder of record on the books of said corporation and reside at 12 Landau Avenue, Elmont, New York.

This affidavit is submitted in support of the multiple Motion to permit me to take the depositions of the plaintiff Dann and the defendants in the above-entitled actions pursuant to Rule 26 and to require said plaintiff and defendants to produce all relevant and material books, records, documents and tangible things.

The Motion further seeks a stay of all proceedings in connection with the proposed settlement of the above-entitled stockholders' suits and to permit me to intervene therein as a party plaintiff.

In my opinion the charges made by Dann and Gallo, if in fact sustained, constitute a national disgrace particularly in view of the fact that Chrysler Corporation is one of the largest business entities in the United States.

I must confess to the Court that my specific knowledge of the charges involved has been derived from a reading of the Dann and Gallo Complaints and from the proceedings in connection with the proposed settlement. I have no personal knowledge of the matters involved nor have I taken any depositions in connection therewith.

My attorneys have advised me that the proceedings heretofore had indicate that the charges made by Dann and Gallo have some basis but that the present record is insufficient to warrant any conclusive determination.

My attorneys have further advised me that the Court's Opinion approving the settlement of the stockholders' liti-

gation involved herein was made on the basis of the record adduced before this Court.

My attorneys have received a telegram from the plaintiff Dann as well as a large number of documents which indicate both to my attorneys and to myself the very serious possibility of fraud in connection with the settlement of the above litigation.

The charges made by Dann are of a very serious nature and, if proven, would warrant, in both my attorneys' opinion and my own, the imposition of the most severe sanctions that this Court could make.

Obviously I cannot, merely on the basis of assertions made by Dann, state categorically that fraud has been involved in the making of the instant settlement. However I would be in a position to do so if I had an opportunity to examine all of the parties concerning all of the relevant facts and circumstances involved in the making of the settlement involved herein.

There appears to be enough in the papers to indicate substantial grounds for believing that fraud has been involved. Therefore I believe that the interests of the stockholders and of justice would be served by permitting me to have the opportunity of taking depositions of all of the parties involved and of requiring these parties to produce all relevant and material documents involving the issues of this litigation.

I realize that this proceeding has been protracted for a considerable period and therefore am willing to agree that, subject to the cooperation of the parties to be examined, that the depositions can be concluded within ninety (90) days. At the conclusion of this period I would be in a position to make an alternative application to the Court for leave to continue this litigation to trial and Judgment, for leave to request the imposition of additional conditions in connection with any settlement of the aforesaid litiga-

tion, or for leave to permit the settlement to go forward on the present basis.

The undersigned regrets that the shortness of time involved in connection with this application prevents the filing of an appropriate Memorandum of Law but I have been advised by my attorneys that wherever there is the slightest possibility of fraud in connection with stockholders' suits the Court must suspend all proceedings until a full and thorough investigation of any allegations of fraud is concluded.

I should be most happy to cooperate with the Amicus Curiae appointed by this Court in order to fully and thoroughly investigate the serious charges that have now been made.

I believe that I probably am a party to the above-entitled litigation by reason of my filing of objections to the settlement thereof. However, in order to remove all doubts, I request that this Court formally grant me the right to intervene as a party and to amend the captions of the actions accordingly.

s/ ARTHUR HOFFMAN.

(Sworn to February 21, 1964.)